

April 26, 2006

The Honorable A.G. Kawamura, Secretary
California Department of Food and Agriculture
1220 N Street
Sacramento, CA 95814

Re: Amendments To Our Petition For The June 1, 2006 Class 2, 3, 4a and 4b Hearing

Dear Secretary Kawamura:

Dairy Institute of California petitioned for a hearing to amend the Class 4a and Class 4b on February 6, 2006. In our petition, we stated our intention to amend our proposed make allowances when the Department's adjusted manufacturing cost averages, reflecting more current energy and labor costs, became available. In addition to updated manufacturing cost information, the Department has published updated data detailing the difference between California weighted average prices for butter and cheddar cheese blocks and comparable prices for those products at the Chicago Mercantile Exchange. It has also published data regarding average fat and nonfat solids tests of producer milk during the most recent calendar year. We have amended our petition in light of the newly available information. The attached extracts of the Stabilization and Marketing Plans for Market Milk for the Northern and Southern California Marketing Areas contain our new proposed changes to Class 4a and Class 4b pricing formulas and comprise Dairy Institute's amended petition for this hearing.

Description of requested changes:

The proposed changes to the Class 4a and Class 4b formulas are shown below. Items that have changed relative to our original petition are ***highlighted***.

Class 4a

Current Formula

Fat = (CME Butter Price - \$0.0285 - \$0.156) x 1.2
SNF = (CA NFDM Price - \$0.152)

Proposed Formula

Fat = (CME Butter Price - ***\$0.0168*** - \$0.156) x 1.2
SNF = (CA NFDM Price - ***\$0.1591***)

A change in the *f.o.b.* price adjuster for butter is proposed because new data released by CDFA suggest that California's weighted average prices for butter averaged **\$0.0168** less than the Chicago Mercantile Exchange (CME) Grade AA spot butter price during the ***January 2004 – December 2005 period***. The proposed make allowance for butter is unchanged from the current formula, because the current make allowance covers approximately 75% of the butter manufactured in the state. We have maintained that the volume covered by the manufacturing allowance should be roughly equivalent across butter, nonfat dry milk, and cheese. Based on the March 2005 hearing decision, the butter make allowance was set higher than the weighted average cost in order maintain equivalent cost coverage with nonfat dry milk and cheese. The manufacturing allowance for nonfat dry milk we propose equals the most recent weighted average cost for making nonfat dry milk, ***adjusted for January- September 2005 utility and labor costs***.

Class 4b

Current Formula

$$\begin{aligned}\text{Cheese CWT} = & (\text{CME 40\# Cheddar Block Price } -\$0.029 - \$0.171) \times 10.2 \\ & + (\text{CME Butter Price } -\$0.10 - \$0.156) \times 0.27 \\ & + (\text{Western Dry Whey Price } - \$0.20) \times 5.8\end{aligned}$$

Fat = Class 4a Fat Price

$$\text{SNF} = (\text{Cheese CWT} - (3.72 \times \text{Class 4b fat price}))/8.8$$

Proposed Formula

1. *Initial Formula*

$$\begin{aligned}\text{Cheese CWT} = & (\text{CME 40\# Cheddar Block Price } -\mathbf{\$0.0252} - \mathbf{\$0.1791}) \times 10.0 \\ & + (\text{CME Butter Price } -\$0.10 - \$0.156) \times 0.27 \\ & + (\text{Western Dry Whey Price } - \mathbf{\$0.2742}) \times 5.8\end{aligned}$$

Fat = Class 4a Fat Price

$$\text{SNF} = (\text{Cheese CWT} - (3.67 \times \text{Class 4b fat price}))/\mathbf{8.8}$$

2. *Permanent Formula (to be employed after the dry whey price falls to \$0.2742 per pound or lower)*

$$\begin{aligned}\text{Cheese CWT} = & (\text{CME 40\# Cheddar Block Price } -\mathbf{\$0.0252} - \mathbf{\$0.1791}) \times 10.0 \\ & + (\text{CME Butter Price } -\$0.10 - \$0.156) \times 0.27\end{aligned}$$

Fat = Class 4a Fat Price

$$\text{SNF} = (\text{Cheese CWT} - (3.67 \times \text{Class 4b fat price}))/\mathbf{8.8}$$

Our proposal changes the *f.o.b.* adjuster for cheese to ***-\$0.0252*** per pound, reflecting the average difference between California and CME cheddar cheese prices during the period

January 2004 – December 2005. The proposed make allowances for cheddar cheese and dry whey are the weighted average manufacturing costs for cheese and dry whey from the most recent CDFA cost surveys, ***adjusted for January-September 2005 utility and labor rates.*** The cheddar cheese yield of 10 pounds per hundredweight of milk testing 3.67% fat and ***8.8% solids not fat*** was obtained using the Van Slyke Cheddar Cheese Yield Formula. The component tests are the average for all California milk during the calendar year ***2005.***

Based on 2000-2005 commodity price data, the proposed changes would have decreased the Class 4b price by an average of 31 cents per hundredweight over the six-year period, while Class 4a prices would have decreased by 1 cent per hundredweight.

Sincerely,

William Schiek
Economist

cc A. J. Yates, Undersecretary
 Kelly Krug
 David Ikari

Northern and Southern California Stabilization and Marketing Plan (Plans 43 and 59), Proposed Changes:

I. Article III - Class Prices

Section 300.0.

(D) The minimum prices to be paid for components used for Class 4a shall be computed as follows:

- (1) For all milk fat, not less than the price per pound computed by the formula using the butter price, less an f.o.b. California price adjuster of ~~two and eighty five hundredths cents (\$0.0285)~~ *one and sixty-eight hundredths cents (\$0.0168)*, less a manufacturing cost allowance of fifteen and six tenths cents (\$0.156), and the result multiplied by a yield factor of one and two-tenths (1.2).
- (2) For all milk solids-not-fat, not less than the price per pound computed by the formula using the nonfat dry milk price, less a manufacturing cost allowance of ~~fifteen and two tenths cents (\$0.152)~~ *fifteen and ninety-one hundredths cents (\$0.1591)*, multiplied by a yield factor of one (1.0).
- (3) The butter prices used in calculations pursuant to this Paragraph shall be the simple average of the Grade AA butter price quotations for the last significant trading action for sale, offer or bid at the Chicago Mercantile Exchange falling between the period beginning the 26th day of the previous month and concluding the 25th day of the current month.
- (4) The nonfat dry milk prices used in calculations pursuant to this Paragraph shall be the weighted average price per pound for all Grade A and extra grade nonfat dry milk for human consumption sold f.o.b. California manufacturing plants for the period beginning the 26th day of the previous month and concluding the 25th day of the current month, as reported by the California Department of Food and Agriculture for the month.
- (5) In the event that the Chicago Mercantile Exchange Grade AA butter price is not available to calculate the current Class 4a fat price, pursuant to Subparagraph (D)(1), then used in its place shall be the Chicago Mercantile Exchange Grade AA butter price used in the prior month's calculation of the Class 4a fat price. All other Paragraphs that use the Class 4a fat price shall operate as if the price had been established pursuant to Subparagraph (D)(1).
- (6) In the event that the California weighted average nonfat dry milk price is not available to calculate the current Class 4a solids-not-fat component price, pursuant to Subparagraph (D)(2), then used in its place shall be the California weighted average nonfat dry milk price used in the prior month's calculation

of the Class 4a solids-not-fat price. All other Paragraphs that use the Class 4a solids-not-fat price shall operate as if the solids-not-fat price had been established pursuant to Subparagraph (D)(2).

(E) The minimum prices to be paid for components used for Class 4b shall be computed as follows:

- (1) The Cheese hundredweight price shall be the price per hundredweight computed by the sum of the following:
 - (a) The price per hundredweight computed by the formula using the Cheddar cheese price, less an f.o.b. California price adjuster of ~~two and ninety hundredths cents (\$0.0290)~~ *two and fifty-two hundredths cents (\$0.0252)*, less a Cheddar cheese manufacturing cost allowance of seventeen and ~~one tenth cents (\$0.171)~~ *ninety-one hundredths cents (\$0.1791)*, all multiplied by a yield factor of ten and ~~two tenths (10.2)~~ *(10)*.
 - (b) The price per hundredweight computed by the formula using the butter price, less a manufacturing cost allowance of fifteen and six tenths cents (\$0.156), less ten cents (\$0.10), all multiplied by a yield factor of twenty-seven-hundredths (0.27).
 - (c) The price per hundredweight computed by the formula using the dry whey price, less a manufacturing cost allowance of twenty-seven and *forty-two hundredths cents (\$0.2742)*, all multiplied by a yield factor of 5.8
 - (d) *If, in any month after May 2006, the dry whey price per pound computed pursuant to Subparagraph (E)(6) is less than or equal to twenty seven and forty-two hundredths cents (\$0.2742), then for such month and every month thereafter, Subparagraph (E)(1)(c) shall cease to be applicable to the computation of minimum prices paid for components used for Class 4b and shall be removed from this Stabilization and Marketing Plan.*
- (2) For all milk fat, not less than the price per pound computed pursuant to Subparagraph (D)(1) of this Section.
- (3) For all milk solids-not-fat, not less than the price per pound computed by the formula using the Cheese hundredweight price established pursuant to Subparagraph (E)(1) less the product of three and ~~seventy-two sixty-seven hundredths (3.72)~~ *(3.67)* multiplied by the Class 4b fat price established pursuant to Subparagraph (E)(2), all divided by eight and eighty hundredths (8.80).
- (4) The Cheddar cheese prices used in calculations pursuant this Paragraph shall be the simple average of the 40 pound block Cheddar cheese price quotations for the last significant trading action for sale, offer or bid at the Chicago Mercantile

Exchange falling between the period beginning the 26th day of the previous month and concluding the 25th day of the current month.

- (5) The butter prices used in calculations pursuant this Paragraph shall be the simple average of the Grade AA butter price quotations for the last significant trading action for sale, offer or bid at the Chicago Mercantile Exchange falling between the period beginning the 26th day of the previous month and concluding the 25th day of the current month.
- (6) The dry whey prices used in calculations pursuant to this Paragraph shall be the simple average of the Dry Whey – West Mostly prices as published in Dairy Market News between the period beginning the 26th day of the previous month and concluding the 25th day of the current month.
- (7) In the event the Chicago Mercantile Exchange 40 pound block Cheddar cheese price is not available to calculate the Cheese hundredweight price, pursuant to Subparagraph (E)(1), then used in its place shall be the cheese price used in the prior month's calculation of the Cheese hundredweight price.
- (8) In the event that the Chicago Mercantile Exchange Grade AA butter price is not available to calculate the Cheese hundredweight price, pursuant to Subparagraph (E)(1), then used in its place shall be the Grade AA butter price used in the prior month's calculation of the Cheese hundredweight price.
- (9) In the event that the Dry Whey – West Mostly price is not available to calculate the Cheese hundredweight price, pursuant to Subparagraph (E)(1), then used in its place shall be the Dry Whey – West Mostly price used in the prior month's calculation of the Cheese hundredweight price.